

# **REPORT TO THE CITY COUNCIL BY THE CITY INTERNAL AUDITOR**

## **AUDIT OF THE CADDO-SHREVEPORT SALES AND USE TAX COMMISSION**

**INTERNAL AUDIT REPORT 210100-06**

**DECEMBER 29, 2000**



**EXECUTIVE SUMMARY**  
**AUDIT OF THE**  
**CADDO-SHREVEPORT SALES AND USE TAX COMMISSION**  
**INTERNAL AUDIT REPORT (IAR) 210100-06**

The purpose of the executive summary is to convey in capsule form the significant issues of the audit report. The executive summary is a vehicle for reviewing the report and should be used in conjunction with the entire report.

**INTRODUCTION**

The primary functions of the Caddo-Shreveport Sales and Use Tax Commission (Commission) are collecting, processing, and remitting sales and use taxes owed the City of Shreveport, Caddo Parish School Board and nine other Caddo Parish taxing authorities; auditing businesses for compliance with the sales and use tax law; and assessing and collecting sales and use taxes from businesses with delinquent accounts.

**OVERVIEW OF SIGNIFICANT ISSUES**

Generally, except as noted within this report, we found management and operations over the Commission to be efficient and effective.

Based on the results of our audit, however, we have identified some administrative, accounting, and information systems issues that management should review to improve controls and operational effectiveness. Our comments address the following concerns:

- The lack of a documented, formal disaster recovery plan that addresses the retrieval of key data center operations in the event of a disaster.
- The need for documenting and organizing administrative and operational activities for the Commission into a formal policies and procedures manual.
- The recommendation to consider hiring additional auditors to increase the amount of revenue generated from audits.
- An inadequate segregation of duties over the processing of many financial transactions.

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***AUDIT OF THE***  
**CADDO-SHREVEPORT SALES AND USE TAX COMMISSION**  
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**OBJECTIVES**

We have completed an audit of the Caddo-Shreveport Sales and Use Tax Commission (Commission). The objective of the audit was to review and evaluate the operational, administrative, and general electronic data processing system controls within the Commission.

**SCOPE AND METHODOLOGY**

Our audit was performed in accordance with applicable generally accepted governmental auditing standards. The scope of internal controls was limited to assessing the general controls surrounding the areas of revenue collection, electronic data processing, expenditure processing, audit effectiveness, budgeting, and contract administration. General audit procedures included:

- Interviewing appropriate personnel.
- Reviewing compliance with established or stated policies and procedures.
- Observing operations and ongoing activities.
- Reviewing records, reports, and other applicable documentation.

This audit was conducted jointly by the Caddo Parish School Board and the City of Shreveport.

**BACKGROUND**

The Commission was created by a joint agreement between the City of Shreveport and the Caddo Parish School Board under the authority of La R.S. 33:2738.54 as an independent agency to collect, enforce, and administer sales and use taxes. The taxing authorities (e.g., City of Shreveport or Caddo Parish School Board) levy the sales and use taxes. Customers pay sales taxes to businesses in Caddo Parish on goods purchased or services received. Use taxes are paid on property that is purchased out-of-state (and no sales taxes have been paid) and brought into Caddo Parish. The Commission registers businesses who must collect the local sales and use tax from customers; provides businesses with information and forms related to sales and use taxes; receives and processes tax reports and records; accounts for and maintains records as required by law; deposits revenue received with the fiscal agent of each taxing authority served; reports revenue collected as required or requested; and enforces compliance with the tax laws by auditing businesses under its jurisdiction.

The Commission is governed by a Board of Commissioners. Membership on the four-member board, which comprises the Chief Administrative Officer and the Finance Director from the City of Shreveport and the Assistant Superintendent of Support Services and Finance Director from the Caddo Parish School Board, is by virtue of the position held with the respective taxing authorities. The Commission presently has an authorized staff of fourteen and these employees

carry out the functions of the entity. The 1999-2000 annual budget for the Commission was \$839,400.

## **CONCLUSIONS/FINDINGS/RECOMMENDATIONS**

The Internal Audit Office appreciates the courtesy and cooperation extended to us during the audit by the Commission. Generally, we found that operational, administrative, and general information systems controls within the organization were adequate.

Based on our audit, however, we have made recommendations to management that may serve to further enhance controls within the Commission. Accordingly, we believe management could improve the control environment and operational effectiveness by implementing the following:

- Formalizing a Disaster Recovery Plan.
- Developing a formal policies and procedures manual.
- Increasing audit staff size.
- Segregating financial duties.
- Reviewing and approving the printout of file maintenance changes.
- Updating computer passwords periodically.
- Obtaining a competitive rate of interest on the overnight investment account.
- Generating computer-processed checks for the general and escrow accounts.
- Instituting a formal training program.
- Documenting and revising job descriptions.

### **1. Formal Disaster Recovery Plan**

**Criteria:** A Disaster Recovery Plan contributes to the assurance of continued operation of the data center activities should the current data center become inoperative. Formal documentation of the plan lessens the risks posed by personnel changes.

**Condition:** An informal Disaster Recovery Plan exists to address actions in the event of a disaster that would interrupt the operations of the data center. However, this plan has never been formally documented.

**Effect:** Specific plans may be lost and/or not carried out in the event of employee changes if the Disaster Recovery Plan continues to be maintained informally.

**Cause:** Plans to address a possible disaster have been informally addressed by the Commission.

**Recommendation:** We recommend that a Disaster Recovery Plan be formalized and established in writing.

**Management Plan of Action:** We agree with this recommendation. Management will develop a formal, written disaster recovery plan before the close of the current fiscal year which ends June 30, 2001.

## **2. Policies and Procedures Manual**

**Criteria:** Documented policies and procedures can improve operations of an organization by providing standards for uniformity in practices, establishing clear lines of responsibility, enhancing accountability, and lessening the threat to continuity posed by employee turnover.

**Condition:** The Commission has not promulgated effective policies and procedures that communicate and clearly define authority and responsibility to employees regarding many of the administrative activities performed for the organization. Specifically, we noted a lack of written policies concerning cash handling; expenditure processing; document initiation, authorization, and approval; bank reconciliations; wire transfers; travel; personnel; vacation and sick time; financial reporting; payroll; confidentiality issues; and other critical tasks and responsibilities.

**Effect:**

- Operations may not be in accordance with mission, goals, and objectives.
- Policies and procedures may be violated.

**Cause:** Management has not assessed the benefits of such a document. In many cases, verbal instructions are given to employees. Furthermore, in the past, a lack of turnover in key positions has resulted in continuity of practices.

**Recommendation:** We recommend management develop and implement a policies and procedures manual which addresses key operations and activities of the organization. This manual should be distributed to employees and would serve as a reference tool for employees seeking guidance on the proper handling of transactions and situations.

**Management Plan of Action:** This recommendation somewhat parallels that contained in the management letter associated with our Audited Financial Statements for year ended June 30, 2000. An employee manual and a policy and procedures manual would contain much duplicate information. We will document our policies and procedures into some sort of manual as time permits and attempt to complete this project by the end of our next fiscal year.

## **3. Increasing Audit Staff**

**Criteria:** Staffing of auditors should be appropriate to assure the Commission is achieving desirable audit coverage and maximum revenue from audits.

**Condition:** The Commission is currently staffed with five auditors. In fiscal year 1998-1999, 105 audits were completed, resulting in \$1,877,411 in audit revenue. Ninety-five (95) audits were completed in 1999-2000, resulting in \$3,221,766 in audit revenue. Thus, revenue per auditor totaled \$375,482 in 1998-1999, and \$644,353 in 1999-2000. Consideration of these numbers and conversations with Commission management support the probability that any additional auditors hired would generate more than enough audit revenue to cover the costs of their employment since, in the past, revenue generated per auditor was more than 10 times (10

X) the average salary of the auditors. The number of audits performed each year comprises 1% of the approximately 9,400 active dealers.

**Effect:** Additional auditors hired should result in increased audit revenue for the Commission.

**Cause:** The Commission is staffed by only five auditors.

**Recommendation:** We recommend that the Commission consider hiring additional auditors in order to increase audit coverage and maximize audit revenue.

**Management Plan of Action:** This recommendation will be presented to the Board of Commissioners for their consideration. Any increase in staffing levels requires Board approval and additional funding which the current budget does not cover.

#### **4. Segregation of Duties**

**Criteria:** A key internal control element dictates that duties should be aligned so that no one individual controls too many critical aspects of a process or transaction.

**Condition:** During our review, we noted that there is an inadequate segregation of duties for processing payroll and general expenditures. For example, we noted that for the payroll account, one employee may post payroll records, generate and distribute checks, sign the checks in the administrator's absence, perform electronic wire transfers, and reconcile the payroll bank account. In addition, for the general and escrow accounts, one individual posts transactions, maintains custody of and writes the checks, and completes deposits.

**Effect:** Increased potential that fraud and abuse could occur and not be timely detected.

**Cause:** Other individuals have not been trained to perform these tasks.

**Recommendation:** We recommend management distribute these financial duties in the payroll, general, and escrow accounts among more employees. For example, we suggest that another employee be trained to reconcile all bank accounts. In addition, duties related to completing deposits could be transferred to another employee.

**Management Plan of Action:** Management plans to review the separation of duties for internal control purposes. The "other individuals" in our office who are qualified to perform these tasks currently have full time positions as outside auditors. To bring them in more than is currently required each month would have a negative effect on their productivity (see recommendations \_3\_). The Board of Commissioners will have to decide if the risk of fraud and abuse is serious enough to justify an additional staff position to fully implement the separation of duties recommended.

## 5. Changing of Security Passwords

**Criteria:** Security passwords should be changed periodically to ensure that only authorized users have access to the system.

**Condition:** Access to computer systems is on a need-to-know basis and is controlled by the knowledge of passwords. However, passwords are not changed after their initial setup. There is a risk of someone other than the authorized user having knowledge of passwords.

**Effect:** Unauthorized access to systems may occur.

**Cause:** Passwords are set up to give initial access only and are not changed periodically.

**Recommendation:** We recommend that passwords be changed periodically to ensure that only the administrators and authorized users have knowledge of their respective passwords.

**Management Plan of Action:** All but a small portion of this recommendation has already been implemented. When our new computer system (presently on order) is installed this recommendation will be fully carried out.

## 6. Investment Interest

**Criteria:** Governmental funds should be maintained in a secure, low-risk, interest-bearing account that provides for the greatest return on investment to an entity.

**Condition:** During our review, we noted that the overnight investment account utilized by the Commission had not earned a competitive rate of interest. Based on a historical comparison of rates earned during the past year (June 1999 -May 2000), we discovered that the Commission's overnight account earned approximately one percent (1%) less than other similar, low-risk, secure accounts. This equates to a potential loss of interest earnings of about \$25,000 for the investment account during the year.

**Effect:** Reduced interest-earnings capacity.

**Cause:** Other options had not been considered as secure investment vehicles for this account.

**Recommendation:** We recommend management consider utilizing other investment vehicles to maintain the Commission's overnight funds. Management did transfer the overnight funds into a money market account, thereby, earning a more competitive interest rate. However, management should also consider placing the funds in other secure investment accounts that may earn a higher interest rate than this money market account.

**Management Plan of Action:** We disagree with this finding and conclusion. We have, in fact, always considered "other options" as secure investment vehicles. We had an analysis of our account at Bank One done last June and were in the process of converting our sweep/investment



account to a money market account before the audit started. This increased earnings on overnight balances by about eighty basis points.

We also started discussing other options and inquiring into the Louisiana Asset Management Pool (LAMP) early this year. Our major concern has been the security of the funds deposited. However, even now our earnings on one escrow certificate is within a few basis points of the rate currently paid by LAMP.

## **7. Computer-Generated Checks**

**Criteria:** When practical and feasible, tasks should be automated to increase efficiency and effectiveness of operations.

**Condition:** Although the Commission's automated financial reporting system has the capability to produce computer-generated checks, all operational and escrow account checks, averaging approximately 50-75 per month, are currently manually completed by employees. In contrast, all payroll checks are automatically generated from this system.

**Effect:**

- Inefficiencies of operations.
- Duplication of effort because the same information must be keyed into the system and manually documented on the actual check.
- Processing inconsistency.

**Cause:** Management has not fully applied this check-generation feature to the general and escrow accounts.

**Recommendation:** We recommend that the Commission consider utilizing the feature of the automated financial system to generate computer-processed checks for the general and escrow accounts. Automatic check generation would reduce time and effort, and also aid in reconciling expenditures.

**Management Plan of Action:** Commission management agrees to consider this recommendation in conjunction with recommendation "4."

## **8. Review of File Maintenance Changes**

**Criteria:** Controls should exist to detect unauthorized changes to sales tax files.

**Condition:** A printout of file maintenance changes is produced for changes to the sales tax files. This printout is not reviewed routinely. Forms that document changes made are reviewed and approved by the Operations Manager after the fact.

**Effect:** Unauthorized changes may be made to files without detection.

**Cause:** Changes have been reviewed through the use of the change form. Changes that are not documented on the form may not be detected.

**Recommendation:** We recommend that controls be strengthened through routine supervisory review and approval of the printout of file maintenance changes.

**Management Plan of Action:** Management agrees to routinely review file maintenance changes and approve the monthly printout. Our new computer system will also track the user making such changes, thus adding additional controls.

## 9. Training and Development

**Criteria:** Effective auditing is constructed on a foundation of technical excellence. One way of ensuring that technical excellence is maintained is by having an effective and consistent training program for employees.

**Condition:** The Commission offers no formalized training and development program by which to keep the audit staff abreast of new and changing audit techniques and development.

**Effect:**

- Possibility of inefficiencies in job performance.
- Possible inadequate identification of training needs.

**Cause:** Management has stated that training opportunities are limited for the specialized sales and use tax auditing field.

**Recommendation:** To help ensure that audits are continually completed in an efficient and effective manner, we recommend a formal training program be instituted. From a generalized auditing perspective, some of the likely benefits of consistent training would be:

- Enhancement of the audit staff's ability to identify and detect fraud and abuse.
- Improvement of the auditors' interviewing and work paper preparation skills.
- Consistency in audit methodology and reporting.
- Improved computer skills.

**Management Plan of Action:** We agree that training and development of the audit staff is advisable and every reasonable effort will be made to maintain a trained staff. However, developing a "formal training program" in an organization consisting of only thirteen full time people (five auditors) is simply not practical. Training modules are presently being developed by the Louisiana Association of Tax Administrators. These will be fully utilized when available.

## 10. Job Descriptions

**Criteria:** Job (position) descriptions serve as a formal record of major duties and responsibilities assigned to a position. Each employee should have an accurate position description that serves as

a basis for recording the responsibility and accountability delegated to an employee and for measuring the employee's performance.

**Condition:** Accurate job descriptions were not available for all employees of the Commission. We noted that job descriptions have not been updated since 1985. Since that time, new positions have been added, other positions have been deleted, while other positions have changed, in some respects, due to new and advancing technology and equipment.

**Effect:**

- Employees may not be aware of what is expected of them and in what way their performance may be deficient.
- Incomplete basis on which to evaluate employee performance.

**Cause:** Other responsibilities have precluded updating the job descriptions.

**Recommendation:** We recommend management develop job descriptions for those positions that have been added to the position roster and revise outdated job descriptions to ensure that they reflect current duties and responsibilities of employees. These job descriptions would document position responsibilities, as well as provide an objective basis on which to evaluate job performance. Additionally, the administrator and all employees should sign and date the respective job descriptions.

**Management Plan of Action:** Updated position descriptions are under development. We plan to have these ready for presentation to the Board in April, at the final quarterly meeting for this fiscal year.

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